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FINAL

October 20, 2010

Revision to original certification dated November 26, 2008, and revision dated November 25, 2009

Subject: Revised Two-Plan Model contract year 2009 rate range development and certification

Dear Ms. Liston:

The California Department of Health Care Services (DHCS) contracted with Mercer Government Human Services Consulting (Mercer) to develop revised actuarially sound capitation rate ranges for use during the last six months of the contract year 2009 Two-Plan contract period. The 2009 Two-Plan contract period began October 1, 2008, and ended September 30, 2009. The revised rate ranges reflect the impact of a legislated policy change implemented by DHCS with an effective date of April 1, 2009, and also other updated program changes not reflected in the original rates but applicable to the rating period. The actuarially sound rate ranges accompanying this letter reflect adjusted rate ranges applicable for the time period from April 1, 2009, through September 30, 2009.

Previously, Mercer developed annual contract year 2009 actuarially sound rate ranges and provided DHCS with a rate development and certification letter dated November 26, 2008, which included an exhibit detailing the contract year 2009 rate ranges. These rates were further revised on November 25, 2009, with the updates associated with the legislative change caused by Assembly Bill (AB) 1422. The revised rate ranges that are the subject of this letter reflect the impact of updates associated with the legislative change caused by AB 1653 and other updated program changes. The overall rate-setting methodology used in the development of these further-revised actuarially sound rate ranges has not changed from the method utilized in the original and subsequently revised, contract year 2009 rate range development.

This letter presents an overview of the analyses and methodology used in Mercer's revised managed care rate range development.

Rate methodology

Overview

The revised capitation rate ranges for the DHCS Two-Plan Model managed care program were developed in accordance with rate-setting guidelines established by the Centers for Medicare and Medicaid Services (CMS).

Base data

There have been no changes made to the base data in the development of the revised rate ranges. If desired, please refer to the November 26, 2008, certification letter for more detail related to the development of the base data.

Other elements

There have also been no changes made to the category of aid groupings, data smoothing methods, trends, prior program changes analyses (with the exception of items noted below), the rate range modeling approach or the application of AB 1422. If desired, please refer to the November 26, 2008, certification letter or November 25, 2009, revision for more detail related to these elements of the certification.

Revisions

Hospital reimbursement increases

As mentioned previously, DHCS is implementing a newly legislated policy change (AB 1653) with an effective date of April 1, 2009. This change is increasing the Medi-Cal fee-for-service (FFS) inpatient payment levels in total approximately 40% and the Medi-Cal FFS outpatient hospital and emergency room payment levels in total approximately 92%. The associated managed care service category increases, being implemented at approximately 60% of the FFS increase levels, are applied to the managed care inpatient, outpatient hospital and emergency room unit costs. The specific program change for inpatient unit costs is 25.9% and the program change for outpatient hospital and emergency room unit costs is 56.7%.

Because of the size of these increases to the hospital unit costs within the capitation rates, the administrative costs and underwriting profit/risk/contingency per member per month

(PMPM) amounts were maintained at the levels established after the implementation of the updated program changes noted below.

Updated program changes

Because the program changes were being updated to institute the impact of the hospital reimbursement increases, the other program changes were also reviewed for potential updates. The main update was related to the provider payment reduction to accurately reflect all of the court injunction activity that impacted these program changes. The prior program changes also did not include the impact of the discontinuation of adult optional benefits that became effective July 1, 2009.

All of these updated program changes created an approximate decrease in the capitation rates of (0.30%). Because of this minor change, the administration components were maintained at their previous PMPM levels. However, the underwriting profit/risk/contingency component of the rates continued to flow through, as in the original rates, as a percentage of premium. This underwriting profit/risk/contingency component is 3.0% at the mid-point, 2.0% at the lower bound and 4.0% at the upper bound.

Rate range certification

In preparing the rate ranges described, Mercer has used and relied upon enrollment, eligibility, claim, reimbursement level, benefit design, and financial data and information supplied by DHCS, its managed care organizations (MCOs) and its vendors. DHCS, its MCOs and its vendors are responsible for the validity and completeness of this supplied data and information. We have reviewed the data and information for internal consistency and reasonableness, but we did not audit it. In our opinion the data used for the rate development process is appropriate for the intended purposes. If the data and information are incomplete or inaccurate, the values shown in this report and associated exhibits may need to be revised accordingly.

Mercer certifies that the revised Two-Plan Model April 1, 2009, through September 30, 2009, rate ranges were developed in accordance with generally accepted actuarial practices and principles, and are appropriate for the Medi-Cal covered populations and services under the managed care contract. The undersigned actuaries are members of the American Academy of Actuaries and meet its qualification standards to certify to the actuarial soundness of Medicaid managed care capitation rates.

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Rate ranges developed by Mercer are actuarial projections of future contingent events. Actual MCO costs will differ from these projections. Mercer has developed these rate ranges on behalf of DHCS to demonstrate compliance with the CMS requirements under 42 CFR 438.6(c) and accordance with applicable law and regulations. Use of these rate ranges for any purpose beyond that stated may not be appropriate.

MCOs are advised that the use of these rate ranges may not be appropriate for their particular circumstance and Mercer disclaims any responsibility for the use of these rate ranges by MCOs for any purpose. Mercer recommends that any MCO considering contracting with DHCS should analyze its own projected medical expense, administrative expense and any other premium needs for comparison to these rate ranges before deciding whether to contract with DHCS.

This certification letter assumes the reader is familiar with the Medi-Cal program, Medi-Cal eligibility rules and actuarial rating techniques. It is intended for DHCS and CMS, and should not be relied upon by third parties. Other readers should seek the advice of actuaries or other qualified professionals competent in the area of actuarial rate projections to understand the technical nature of these results.

If you have any questions on any of the above, please feel free to contact Mike Nordstrom at +1 602 522 6510, Jim Meulemans at +1 602 522 8597 or Branch McNeal at +1 602 522 6599.

Sincerely,

A handwritten signature in blue ink that reads 'Michael E. Nordstrom' followed by 'ASA, MAAA' in a smaller, less legible script.

Michael E. Nordstrom, ASA, MAAA

A handwritten signature in blue ink that reads 'James J. Meulemans' followed by 'ASA, MAAA' in a smaller, less legible script.

James J. Meulemans, ASA, MAAA

MEN/JJM/lgm

Copy:
Stuart Busby, DHCS
Gary McHolland, DHCS
Sundee Easter, Mercer
Branch McNeal, Mercer